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HOUSING SUBSIDIES IN CANADA: WHO BENEFITS?

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Introduction

The production and distribution of housing in Canada has been conducted largely through private market mechanisms relying on profit motives. Only a small proportion of Canada's housing stock is owned by government or by non-profit associations.

This does not mean that the private housing industry functions without huge government subsidies. There are major housing subsidies, mainly through tax expenditures, which support housing in general, and owner-occupied housing in particular.

"Tax expenditures" are indirect and hidden forms of government subsidies. The government "spends" money by not collecting it in the first place, through mechanisms such as special tax exemptions, deductions, credits, exclusions, preferential rates and tax deferrals. Tax expenditures, therefore, consist of departures from the generally accepted tax norm, which result in revenue losses for the public sector.

In his October 1980 budget speech, Finance Minister Allan MacEachen noted that tax expenditures "are expensive and it is incumbent on government to ensure that the incentives are effective and their cost is justified." He questioned "whether the economy might not be better served by a tax system with lower rates but with fewer and more selective incentives."

It is not widely understood that the combined amount of the housing-related tax expenditures far exceed the total housing assistance provided to low and moderate income groups under the National Housing Act.

CHF will be publishing a detailed paper on housing-related tax expenditures. Listed below is a summary of some of the issues this paper will examine.

Housing Tax Expenditures Compared to National Housing Act Subsidies

- o Using 1980 as an example, the Department of Finance and CMHC has estimated that housing-related tax expenditures totalled $8.9 billion while direct NHA subsidies totalled $700 million.

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- o Direct NHA expenditures on housing programs therefore equal only 8% of the indirect housing-related tax expenditures.

- o The non-profit and co-op housing programs represent only 0.4% of tax expenditures and 5% of total NHA housing program expenditures.

- o See Tables 1 and 2 for a summary of the above information.

Who Benefits From Tax Expenditures in General

- o Housing-related tax expenditures are only one form of this type of tax syste subsidy. Who benefits from tax expenditures in general?

- o For the 1979 tax year, the Department of Finance prepared estimates of the dollar value of tax expenditures to different income groups. The estimates for five income ranges are reproduced below. They clearly show that the higher the income, the greater the benefit.

Income Group	$ value of 1979 Tax Expenditure Benefit
$ 5,000 - 10,000	$ 460
15,000 - 20,000	1,300
25,000 - 30,000	2,700
50,000 - 100,000	9,900
100,000 and over	46,000

- o The Department of Finance has also estimated that, in 1979, 23% of all tax expenditure subsidies went to individuals earning over $100,000. These individuals represent less than 1% of the tax-filing population.

- o The rapid growth in the use of tax expenditures as a form of government spending has resulted in a shift of the tax burden away from corporations, toward individuals. In 1950, 23% of all federal revenue came from corporate income tax, and 20% came from personal income tax. By 1979, the corporate contribution dropped to 10.3% and the amount contributed by individuals rose to 37%. The corporate tax rate is supposed to be 46% but, on average, the effective corporate tax rate is 25%. The larger corporations pay even less. This same relationship holds for individuals. Upper-income Canadians pay a lower effective tax rate than the average Canadian due to tax expenditures.

Rental Housing Tax Expenditures

- o There have been three main forms of tax expenditures applied to rental housing:

  - Capital Cost Allowance. Introduced in 1949, this provision enables owners of real estate to deduct a depreciation expense (a capital cost allowance) far exceeding the actual or book value depreciation of the property.

    While the difference between actual depreciation and claimed CCA must be paid back upon disposition of the property, the CCA represents an interest-free loan to the developer, paid back in inflated dollars or at a time when the investor is in a lower tax bracket.

- Multiple Unit Residential Buildings (MURBS). This is a special form of CCA allowing investors to deduct depreciation "losses" from all other taxable income, not just from taxable income generated by similar real estate properties.

  This program applies to certified rental buildings started between November 1974 to December 1979, and October 1980 to December 1981.

- Soft Cost Deductability. This allows investors to deduct certain "first time costs" in the year they are incurred, rather than capitalizing them into the building value and depreciated over time through CCA.

o Between 1976 and 1980, these tax expenditures have cost the Canadian taxpayer $825 million. The amount has been increasing dramatically: from $95 million in 1976 to $270 million in 1980.

o It is estimated that MURBs, CCA and soft costs tax expenditures have, for the most part, produced units which rent at the high end of the market.

o High income individuals benefit the most from these rental housing tax expenditures. MURBs, for example, provided an average deduction of $13,000 for individuals earning over $50,000.

Homeownership Tax Expenditures

o There are three major tax expenditures related to ownership housing:

- Registered Homeownership Savings Plan (RHOSP). Begun in 1974, RHOSP allows taxpayers who have never owned a home to save $1,000 per year and to deduct this amount from their taxable earnings.

- Non-Taxation of Capital Gains on Principle Residence. Capital gains associated with the sale of an owner-occupied residence are completely exempt from tax.

- Non-Taxation of Imputed Rent. Homeowners accumulate a tax-free benefit in the form of "imputed rent", which is the difference between the market value of a home less the expenses of homeownership.

o Between 1976 and 1980, these forms of tax expenditures have averaged $6.8 billion dollars per year. They have increased from about $6 billion in 1976 to $8.6 billion in 1980.

o This form of housing subsidy is only available to anyone able or willing to own a home.

o For the growing number of people unable to purchase a home, they are denied access to this form of housing subsidy, yet help pay for it though their income taxes.

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Summary

- The large number of tax expenditures undermine the assumed progressive nature of the tax system. Substantial benefits are being delivered to high income individuals and corporations, rather than distributing the tax burden according to each individual's ability to pay.

- Low and moderate income Canadian households have access to very few of the hidden subsidies provided through the federal government's system of tax expenditures.

- Indirect housing subsidies provided through housing-related tax expenditures benefit mainly upper-income individuals, corporate investors and homeowners. There are few direct benefits for renters and the indirect benefits to renters are extremely limited.

- Direct National Housing Act housing subsidies available to low and moderate income Canadians represent a very tiny percentage of total housing-related tax expenditures.

- In 1980, the social housing and public housing subsidies combined equalled $300 million, about 4% of total housing-related tax expenditures.

- Low and moderate income Canadians help pay for all forms of housing subsidies, yet benefit the least. This helps explain why there has been virtually no redistribution of income over the past 30 years, in spite of the growth of the "welfare state" and a "progressive" income tax system.

- Because of the huge level of housing-related tax expenditures, most of which are targeted at upper income groups, direct NHA expenditures on social housing programs should be expanded as a means of directing a more equitable share of housing subsidies to low and moderate income Canadians.

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TABLE 1

Estimated Federal Housing-Related Tax Expenditures

1979, 1980 ($ millions)

Rental Housing[1]	1979	1980
Use of CCA rather than actual depreciation*	$ 61	$ 65
MURB provision**	95	95
Deductibility of soft costs	65	110
Ownership Housing[2]		
RHOSP	95	95
Non-taxation of capital gains on principle residence	3,000	3,500
Non-taxation of imputed rent	4,000	5,000
TOTAL	$7,316	$8,865

Notes: * This figure represents the total stock of rental dwellings which are being depreciated.

** This assumes a federal marginal tax rate of 36 percent and does not include the amount of provincial taxes lost.

Sources: 1. Clayton Research Associates (1981) Tax Expenditures - Housing, Ottawa: Canada Mortgage and Housing Corporation.

2. Canada, Department of Finance (1980) Government of Canada Tax Expenditure Account, Ottawa.

TABLE 2

NHA Housing Program Expenditures

1979, 1980 ($ millions)

	1979	1980
AHOP	33.1	29.0
RRAP	97.1	106.8
Home Insulation	77.9	212.9
Emergency Repairs	1.5	1.1
Public Housing	265.4	262.7
Non-profit & Co-op	25.6	34.8
Community Resource Groups	6.6	8.2
Interest & Lease Losses	19.5	18.9
ARP	11.5	25.0
TOTAL	538.2	699.4

Source: CMHC, Annual Reports, 1980, 1981.